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Author(s): Wemple, Erik C.

Abstract: Talks about the difficulty faced by the United States in developing *export* control policies for Hong Kong and China. Logic behind *export* controls; China's diminished usefulness as a strategic ally to the United States; Strict *export* controls system in Hong Kong; Hesitation of the US to ease restrictions on high-technology shipments to China. INSET: A decade of *export* control policy for China.

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AN *EXPORT* CONTROLS CLASH

Western *export* control policies for Hong Kong and China are on a collision course

While the growing economic interdependence of Taiwan, China, and Hong Kong may be a boon to US companies seeking a foothold in the dynamic Greater China region, it will probably prove a bane to US officials in charge of *export* control policy. Confronted by an evolving world order in which economic competition is fierce and military alliances are no longer rigid, these officials will undoubtedly find it increasingly difficult to develop any coherent approach to *export* controls. The blurring boundaries between Hong Kong, China, and Taiwan--which are afforded very different treatment under the current US and international *export* control regimes--will only make their task more challenging.

A changing picture

Limits on the transfer of US technology abroad are essentially established by the US *Export* Administration Act and the Coordinating Committee for Multilateral *Export* Controls (COCOM), an over-arching international body consisting of Japan, Australia, and all NATO countries except Iceland. The logic behind *export* controls is to limit the transfer of technology with potential military applications to countries perceived as unfriendly or unreliable. *Export* controls are also used--especially by the United States--as "carrots" or "sticks" with which to achieve foreign policy objectives. To be effective, *export* controls must be clearly defined, multilaterally implemented, and carefully monitored. To maintain such a policy for China will prove daunting, as US and foreign perceptions of the country--and of Hong Kong and Taiwan--are undergoing profound change.

As Western concern over the former Soviet Union and its influence has eased, China's usefulness to the United States as a strategic ally has diminished. More attention, therefore, is being paid to other facets of the Sino-US relationship, such as human rights, trade, and arms proliferation issues, especially since the Tiananmen crackdown of 1989. Increasingly, the United States seems to view China as a ***rogue*** element in the international arena and is striving to make it conform to international norms in each of these three areas. One of the chief methods employed by Washington to encourage changes in Beijing's behavior has been the imposition of sanctions on the sale of various high-tech items to China.

The same forces that have increased tension between the United States and China, however, have worked to decrease it between the United States and Hong Kong and Taiwan. Taiwan has significantly liberalized its political and economic systems and has reduced its trade surplus with the United States by about $6 billion over the past five years. Hong Kong-US trade has also become more balanced, and US officials have taken a number of steps to help safeguard the territory's democratic and capitalist base in the years preceding and following its reversion to Chinese sovereignty in 1997 (see p. 11). In contrast to China, for which the United States has sought to limit access to advanced technology and weaponry over the last few years, Taiwan and Hong Kong have seen restrictions on technology transfer eased, either intentionally or through general relaxations in their country groupings.

While political differences between Taipei and Beijing remain acute enough to prevent significant transfers of advanced technology from Taiwan to the mainland in the near term, the same cannot be said about Hong Kong. Impending Chinese control over the territory calls into question whether current US and COCOM policy to delineate between the two is realistic. And should China use its future power as administrator of Hong Kong to circumvent the territory's ***export*** control regulations, the risks are high: China could channel such technology to the production of missile delivery systems, which it might then sell to such unstable regions as the Indian subcontinent and Middle East.

Easing sales to Hong Kong

According to the 1984 Sino-British Joint Declaration on Hong Kong, when the territory becomes a "special administrative region" of China in 1997, it will retain its status as a separate customs territory. As such, it will be able to negotiate and implement its own trade arrangements with the rest of the world. Since management of ***export*** controls is a routine function of a customs territory, the declaration implicitly recognizes Hong Kong's right to develop and maintain regulations on shipments of high-technology items to other areas, including China.

As a colony of the United Kingdom, Hong Kong has long maintained a strict ***export*** controls system that conforms with the standards established by the British government and the multilateral trade control regimes in which it participates. Hong Kong's ***export*** control bureaucracy is a reflection of the UK model, for it features separate offices for key ***export*** control functions such as commodity classification, license review, and ***export*** ennforcement.

To ensure that its controls match those of COCOM member countries, Hong Kong has adopted and implemented the three official COCOM commodity control schedules: the Industrial List, the International Munitions List, and the International Atomic Energy List. Of these, the COCOM Industrial List has the greatest impact on Hong Kong's trade because it covers a wide universe of high technology dual-use items--those with both commercial and military applications--that pass in high volume through the territory. The Industrial List outlines controls on the following categories of advanced dual-use goods: materials, materials processing (machine tools), electronics, computers, telecommunications and cryptography, sensors, avionics and navigation, marine technology, propulsion systems, and

transportation equipment.

In accordance with COCOM policy, Hong Kong must control all Industrial List items to countries traditionally viewed by COCOM members as potential threats to Western security: the former republics of the Soviet Union, Czechoslovakia, Hungary, Poland, Albania, Bulgaria, Romania, Mongolia, and China. The controls vary from basic application procedures for easily obtained licenses to thorough investigations of potential endusers. Through the UK COCOM delegation, Hong Kong submits license applications for ***exports*** of the most advanced COCOM-controlled goods to these destinations to the committee for review.

Furthermore, Hong Kong has implemented controls on items useful in the production of missile delivery systems, as well as chemical, biological, and nuclear weapons. These controls, which cover low- to medium-technology goods and apply to countries of proliferation concern in the developing world, extend beyond the purview of COCOM ***export*** regulations and are instead modeled after the regulations of three international proliferation control regimes: the Missile Technology Control Regime (MTCR, for missile delivery systems), the Australia Group (AG, for chemical and biological weapons) and the Nuclear Non-Proliferation Treaty/Zangger Committee (NPT, for nuclear weapons).

Each of these regimes, like COCOM, has developed a standard control list to which member countries are obligated to adhere. Although Hong Kong is not an official member of these proliferation control regimes, it has adopted their control lists in its domestic ***export*** control regulations. To observe the guidelines of these regimes, Hong Kong must place strict controls on ***exports*** of all MTCR, AG, and NPT commodities to China. Such commodities include:

• MTCR: rockets, air vehicles and subsystems, propulsion components, missile structural composites, launch and ground support equipment and facilities, and dual-use items helpful in missile design and production;

• AG: 50 chemicals with applications in the production of chemical and biological warfare agents;

• NPT: uranium enrichment equipment and technology, nuclear-grade graphite, and other materials and technology designed for nuclear applications.

In recognition of Hong Kong's progress in establishing a domestic ***export*** control system, the United States and other COCOM countries are preparing to accord the territory "associate" COCOM member status. According to US Department of Commerce (DOC) officials, a regulatory amendment instituting licensing relaxations for Hong Kong commensurate with associate status will become effective as The CBR goes to press in mid-April. Under this arrangement, Hong Kong will enjoy the same US ***export*** licensing privileges as such countries as Ireland, Switzerland, Sweden, Austria, and Finland. Basically, the implementation of associate status will result in the elimination of validated licensing requirements for ***exports*** of nearly all US-origin COCOM-controlled dual-use commodities to Hong Kong.

In practical terms, the regulatory change expands the range of high-technology goods that US ***exporters*** and foreign re-***exporters*** may send to Hong Kong without filing license applications with the DOC. The relaxation will apply to all integrated circuits, most advanced telecommunications equipment and machine tools, and all computers except supercomputers. The list of items excluded from this treatment is short and covers products of little commercial importance such as surreptitious listening devices, encryption technology, and certain state-of-the-art cameras. The UK has already implemented a set of similar licensing benefits, and other COCOM countries may soon follow the leads of Britain and the United States in this regard.

Receiving asssociate COCOM-member treatment should stimulate Hong Kong's trade in high-technology goods. The drastic reduction in the United States' burdensome licensing requirements will undoubtedly act as a strong incentive for companies in COCOM countries to develop stronger trade ties with Hong Kong, both in the form of ***exports*** and direct investment. According to Eric L. Hirschhorn, an expert on overseas investment and trade with the Washington law firm of Winston & Strawn, "Dramatic reductions in ***export*** licensing requirements--such as the one in store for Hong Kong--often have a direct and tangible impact on business decisions by internationally integrated high-technology companies." Hirschhorn notes that computer companies, which are tightly regulated by COCOM ***export*** curbs and often source components from facilities in Asian countries, would be most likely to take full advantage of the changes.

Clamping down on China

While the United States and other COCOM members are moving to liberalize ***export*** controls for Hong Kong, they remain hesitant to ease current restrictions on high-technology shipments to China. Virtually all developed countries imposed sanctions forbidding the sale of weapons and military goods after Tiananmen, and the United States added further sanctions against the transfer of certain high-technology items in June 1991. These later sanctions were imposed to punish Chinese firms thought to be violating international arrangements governing sales of missile-and nuclear-related technology. China has since agreed to adhere to both the NPT and the MTCR, prompting the United States in March to rescind its June 1991 sanctions.

Despite China's recent swing toward cooperation with multilateral arms-control efforts, controls on ***exports*** to China under COCOM and MTCR continue to reflect serious concerns about China's military capabilities and proliferation activities. COCOM member countries still require individual validated ***export*** licenses for all shipments to China of items on the three COCOM lists. This policy allows licensing authorities in each member country to conduct a thorough review of the Chinese customer and the proposed end use of every proposed shipment of COCOM-controlled items.

A detailed set of commonly agreed-upon guidelines governs the standard of scrutiny that member countries apply to any given shipment of a COCOM-controlled commodity to China. For example, member countries have implemented a policy of "extended review or denial" for license applications involving goods and technology related to nuclear weapons, electronic and antisubmarine warfare, intelligence gathering, power projection, and air superiority.

On the other hand, low-level COCOM commodities are treated to a "presumption of approval" policy, under which member-country governments expedite the processing of license applications and block shipments only under extraordinary circumstances. Examples of commodities qualifying for this licensing treatment include computers with a Composite Theoretical Performance (CTP) not exceeding 20 million theoretical operations per second (Mtops) and international fiber-optic telecommunications systems with transfer rates not exceeding 156 megabits (Mbits)/second. The DOC often processes presumption of approval cases in less than two weeks; there is no COCOM plenary review for these cases.

COCOM regulations stipulate a policy of "favorable consideration" for the intermediate tier of COCOM-controlled technology outlined in the Industrial List. All ***export*** license applications in this category receive thorough scrutiny by member countries--in the United States, the DOC refers all such cases to the ***Defense*** Department for review--and an often protracted COCOM plenary review. COCOM ***exporters*** may have to endure a wait of two months for approval of sales of goods in this category.

Export applications for items that exceed the parameters for presumption of approval and favorable consideration are reviewed on a case-by-case basis. As might be expected, individual country and COCOM review of these cases is more thorough than for special category cases.

Since COCOM vamped its Industrial List in 1991, it has displayed an unwillingness to consider further liberalization of restrictions on trade with China. For instance, in March several key COCOM countries--the United States, United Kingdom, Germany, France, Japan, and Italy--negotiated a new telecommunications agreement, but decided to explicitly exclude China from eligibility for any control relaxations. Similar future reviews of controls on computers and other Industrial List categories may also differentiate between China and other COCOM-proscribed destinations.

The licensing policies of MTCR member countries for ***exports*** to China are straightforward and do not provide for varying scrutiny standards on the basis of technology levels. All MTCR countries--and particularly the United States--perform a separate, extensive license review for ***exports*** of missile-related items to China. Since all such ***export*** applications are viewed suspiciously by licensing authorities, ***exporters*** in MTCR countries bear the burden of proving that the ***export*** commodity is destined for an exclusively civilian application.

The widening technology gap

The strict COCOM and MTCR licensing policies for China contrast sharply with the corresponding treatment that Hong Kong receives under the guidelines of these regimes. After the United States formally implements associate COCOM status for Hong Kong, for instance, US companies may ***export*** computers with CTPs under 196 Mtops to Hong Kong without filing for an individual validated license with the DOC. These ***exporters*** will be able to take advantage of the DOC's General License for COCOM Trade (GCT) authorization, which enables US ***exporters*** to ship nearly all COCOM-controlled commodities to COCOM and associate COCOM countries without submitting license applications.

However, no such general license authorization exists for shipments of US-origin commodities to China. Current COCOM-based US control policies for China--which are unlikely to change in the near future--dictate that any computer with a CTP exceeding 12.5 Mtops requires an individual validated ***export*** authorization. Although the special treatment provisions of the COCOM regulations allow for expedited and favorable review at certain levels above the 12.5 Mtops mark, the United States and COCOM member countries have the opportunity to review--and thus deny--shipments to China that will proceed without any license review whatsoever to Hong Kong.

Although the MTCR control guidelines require licenses for shipments of missile-related commmodities to any destination, the license review process for such ***exports*** from member countries to Hong Kong is perfunctory. For example, when reviewing an application from a US aerospace company to ***export*** an airborne radar system (an MTCR-controlled item) to a Hong Kong entity, the DOC would make a routine check to ensure that the proposed end use was legitimate and that the Hong Kong buyer had not been previously involved in illicit missile technology diversions. If this review produces no red flags, the ***exporter*** could expect approval in less than two weeks.

An ***export*** application for the same item to a Chinese entity would likely be subject to scrutiny by an array of offices and inter-agency committees throughout the vast US foreign trade and ***national*** security bureaucracy. In such a case, the US ***exporter*** should expect a lengthy processing period and, at the end of it, possible denial of the license.

In fact, the routine US licensing guidelines for ***exports*** of missile-related items to China are so strict that the special missile control sanctions imposed by the Bush Administration in 1991 had little practical effect on US technology transfers to China. These sanctions imposed new controls on high-level computers and satellites and a policy of denial for sales of missile-related items to two Chinese companies notorious for their involvement in overseas missile projects (see box). Under current MTCR and COCOM regulations, all items to which the sanctions applied already required a validated license for ***export*** to China; the United States thus would likely have denied license authorization for these ***exports*** even in the absence of the sanctions.

The incentive for China to subvert Hong Kong's ***export*** control regime post-1997 and use the territory as a high-tech shopping mart is considerable. US ***export*** control officials, however, appear reluctant to consider this possibility. When asked how the United States would respond if such a situation develops, a State Department official involved in Hong Kong trade issues responded, "Since I can't recognize the existence of a problem, I can't offer a possible solution." A policy-level official in the DOC's Bureau of ***Export*** Administration, the agency that handles the licensing of US dual-use ***exports***, conceded that Chinese interference with Hong Kong's Customs administration would pose a serious ***export*** control problem for the United States, but indicated that no one has yet formally addressed the issue.

Instead of waiting for the problem to occur, the United States and other COCOM countries should explore ways to discourage Chinese meddling in Hong Kong's system of ***export*** controls in order to prevent a crisis from developing. Otherwise, the responses that might be adopted to reduce Chinese infringement--such as the imposition of trade and economic sanctions against China or the downgrading of Hong Kong's (and therefore China's) access to COCOM technology--could have dire consequences for China, Hong Kong, and US companies alike.

The best way to prevent this scenario from occurring involves nurturing a responsible Chinese approach to international technology transfer. China's leaders recently took significant steps in this direction by acceding to the NPT and declaring in principle their willingness to adhere to the MTCR. As previous Chinese commitments along these lines have not led to the implementation of concrete measures to halt illicit shipments of missile- and nuclear-related items, however, most Western governments are still somewhat skeptical of China's intentions.

Therefore, the United States and other developed countries must carefully monitor China's progress in establishing the domestic mechanisms that are essential for compliance with its new obligations under these control regimes. China must create the necessary administrative framework--based largely upon the models of COCOM- and MTCR-member countries--to educate ***exporters*** about the new controls, review ***export*** license applications, and punish firms that violate the controls. Clearly, implementing these regulatory steps will be difficult for the current Chinese leadership, which has historically promoted ***exports*** of weapons technology in order to earn desperately needed hard currency.

Nevertheless, if China successfully adopts such measures, the payoff could be great. The dramatic change in China's ***export*** control policies would enable COCOM- and MTCR-member countries to narrow--and perhaps eventually close--the current gap in technology access between China and Hong Kong. Thus, China, Hong Kong, and Western ***exporters*** all stand to benefit substantially from China's compliance with its recent non-proliferation commitments--a fact that foreign governments and companies should emphasize in their dealings with the Chinese to ensure that Beijing clearly understands the potential costs and benefits of its actions.

US *Export* Controls for Greater China

The following chart reads as follows:

Row 1: Commodity

Row 2: Taiwan

Row 3: Hong Kong[a]

Row 4: China

Dual-use Non. MTCR Items

-- computers

</= 20 Mtops: No individual validated license (IVL) required
> 20 Mtops: IVL required. Presumption of approval applies

</= 195 Mtops: No IVL required
> 195 Mtops: IVL required. Presumption of approval applies

</= 12.5 Mtops: No IVL required
> 12.5 </= 20 Mtops: IVL required. Presumption of approval applies
> 20 </= 23 Mtops: IVL required. Favorable consideration applies
>23 Mtops: IVL required. Considered on a case-by-case basis

-- telecommunications transmission equipment

</= 156 Mbits/sec: No IVL required
> 156 Mbits/sec: IVL required. Presumption of approval applies

No limits
No IVL requirements

</= 45 Mbits/sec: No IVL required
> 45 </= 156 Mbits/sec: IVL required. Presumption of approval applies
> 156 </= 565 Mbits/sec: IVL required. Favorable consideration applies
> 565 Mbits/sec: IVL required. Considered on a case-by-case basis

-- machine tools

> 4 interpolating axes: IVL required. Presumption of approval applies

No limits
No IVL requirements

> 4 interpolating axes: IVL required. Considered on a case-by-case basis

Munitions Control List Items

-- launch vehicles
-- firearms
-- military vehicles
-- military aircraft engines
-- military & space electronics

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-- military-related technical data

      Munitions license required.
      Considered on a case-by-case basis

      Munitions license required.
      Considered on a case-by-case basis

      Prohibited

MTCR Items[b]

-- propulsion components
-- composites
-- flight instruments
-- launch/ground support facilities
-- inertial navigation systems

      IVL required. Presumption of approval applies

      IVL required. Presumption of approval applies

      IVL required. Considered on a case-by-case basis
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a All entries for Hong Kong reflect associate COCOM-member status.

b MTCR items also on the Munitions Control List (MCL) are subject to the controls listed under the MCL.

Compiled by Erik C. Wemple

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By Erik C. Wemple

Erik C. Wemple is the editor of ***Export*** Control News and a consultant for MK Technology-Deltac, a Washington, DC-based ***export*** management firm. He holds a B.A. from Hamilton College and an M.S. in foreign service from Georgetown University.

Inset Article

A DECADE OF *EXPORT* CONTROL POLICY FOR CHINA

Under the legislative authority of the ***Export*** Administration Act of 1979, the Commerce Department's Bureau of ***Export*** Administration (BXA) administers controls on ***exports*** of a wide range of dual-use goods and technologies to China. These controls are outlined in the ***Export*** Administration Regulations (EAR), which codify licensing requirements according to the ***export***'s technological sophistication and country of destination. These regulations are based in large ***part*** upon agreements that the United States reaches with its partners in the Coordinating Committee on Multilateral ***Export*** Controls (COCOM). Over the past decade, the United States and COCOM have implemented numerous significant changes in ***export*** control policy for China, as described below:

1983: The Department of Commerce implements two measures to upgrade China's ***export***
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licensing status. First, it places China in country group V, which includes friendly, non-aligned countries in Africa, Asia, and Europe. Second, it issues a list of seven technology categories eligible for expedited and favorable review for shipment to China.

1985: COCOM implements a similar set of licensing preferences for ***exports*** from member countries to China. Specifically, the new policy allows authorities in member countries to process license applications for 27 commodity areas with a presumption of approval. In addition, plenary COCOM reviews of ***export*** license applications that qualify for this policy are eliminated. COCOM refers to the new favorable treatment policy as the China "green zone."

1986: COCOM adds three commodity areas to the list of goods and technologies eligible for green zone treatment.

1987: COCOM significantly liberalizes the ***export*** licensing parameters for products that qualify for green zone policy and adds two additional commodity areas to the green zone list. Applications that receive green zone treatment account for over 70 percent of China applications received by BXA.

1988: The Omnibus Trade and Competitiveness Act, passed by Congress in August 1988, mandates the establishment of distribution licenses for China. The distribution license allows US ***exporters*** to make bulk shipments to pre-approved customers in a pre-approved sales territory.

COCOM further liberalizes the technical parameters outlining eligibility for green zone treatment.

1989: China's brutal repression of the Tiananmen Square protests results in the imposition of a munitions embargo by most Western governments and a moratorium on further liberalization initiatives by COCOM. The United States suspends efforts to complete the implementation of distribution license benefits for China.

1990: COCOM countries eliminate licensing requirements for certain dual-use commodities with diminishing military applications to all controlled countries, including China. However, the liberalization does not affect China green zone commodities.

1991: COCOM approves the most dramatic deregulation of dual-use goods and technologies in its 42-year history and introduces a streamlined control list format. As in 1990, the decontrol eliminates licensing requirements for low-level items for ***export*** to China as well as to other COCOM-proscribed destinations, but does not extend the number of goods qualifying for green zone treatment for China.

To signal its disapproval of China's missile proliferation activities, the Bush Administration announces on June 16 a set of special ***export*** controls on satellites and high-performance computers and sanctions on two Chinese entities--the China Precision Machinery Import-***Export*** Corp. and the China Great Wall Industry Corp.--involved in sensitive overseas missile projects.

1992: After receiving assurances from Chinese Foreign Minister Qian Qichen on China's intentions to adhere to the Missile Technology Control Regime (MTCR), the US drops the June 1991 controls and sanctions.

In March, several key COCOM member countries decide to exclude China from eligibility for a landmark liberalization of international telecommunications ***export*** controls.

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By Erik C. Wemple

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